

Micro Enterprise Development Strategy

Strategic Objective No. 4, Sustainable
Increases in Household Income and Food
Security

*Intermediate Results No. 2, More Micro entrepreneurs expanding
Their Businesses*



• MICROENTREPRENEURS SELLING IN FRONT
OF THE PRESIDENTIAL PALACE

TABLE OF CONTENTS

1	<i>Social-Economic Indicators</i>	1
1.1	Distribution of Income:	1
1.2	GINI Index:	1
1.3	Adult Illiteracy Rate:	2
1.4	Land Distribution:	2
1.5	Malnutrition	2
2	<i>Relationship to USAID's and Mission's Strategy</i>	3
2.1	Agency and Bureaus Goals	3
2.2	Missions Strategic Objective (SO) No. 4	4
2.3	The Institutional Intermediaries and Clients	5
2.3.1	Financial Intermediaries	5
2.3.2	The Clients (Micro Enterprises)	7
2.3.3	Geographical Coverage	8
3	<i>Major Constraints Faced by Microfinance Intermediaries</i>	8
3.1	PVOs:	8
3.1.1	Institutional and Financial Sustainability:	8
3.1.2	Focus:	9
3.1.3	Access to Financial Resources and Regulatory Constraints:	9
3.1.4	Interest Rate Ceilings:	9
3.2	FENACOAC	9
3.2.1	Institutional Development:	10
3.2.2	Methodology:	10
3.2.3	Treasury:	10
3.3	Commercial Banks	10
4	<i>Constraints Faced by Micro Enterprises:</i>	11
5	<i>USAID's/G-CAP Vision, Objective, Strategy, and Activities</i>	11
5.1	Vision:	11
5.2	Objectives of the USAID/G Strategy:	11
5.3	Reforming and strengthening the Microfinance Intermediaries (PVOs)	12
5.3.1	Rating System	12
5.3.2	Self-regulating System	13
5.3.3	Incentive Fund	13
5.4	FENACOAC	14
5.4.1	Role as Rating and Supervisory Agency:	14
5.4.2	Methodology:	14
5.4.3	Treasury, New Financial Products and Observation Trips:	14
5.5	Attract Commercial Banks into Microfinance	15

5.6	Other Policy Dialogue and Activities:	16
5.6.1	Influencing Reforms in the Financial Sector	16
5.6.2	Promoting Product Development and New Financial Services	17
5.6.3	Developing Linkages with the Capital Markets	17
5.6.4	Promoting Research and Key Studies	18
5.6.5	Training to Microfinance Trainers	18
5.6.6	Promote Donor Coordination	19
6	<i>ILLUSTRATIVE BUDGET</i>	19
7	<i>ATTACHMENT A: ELEMENTS OF THE INCENTIVE FUND</i>	21
7.1	Objectives:	21
7.2	Focus of the Incentive Fund	21
7.3	Major Aspects of the Methodology:	21
7.4	Institutional Contractor	22
8	<i>ATTACHMENT B: BANRURAL</i>	23
8.1	BANDESA/BANRURAL Background:	23
8.2	Issues:	24
8.2.1	Level the Playing Field:	25
8.2.2	BANRURAL's Strategy:	25
8.2.3	Ownership of Funds:	26
	<i>ATTACHMENT C: ILLUSTRATIVE BUDGET</i>	29
10	<i>ATTACHMENT D: MAP OF 12 MARKET TOWNS</i>	31

1 Social-Economic Indicators

Guatemala is the largest economy of Central America accounting for over one third of the regional gross domestic product (GDP) and about 35% of its total population. Guatemala however faces serious problems of poverty and income inequality. Poverty is mostly concentrated in the rural areas where most of the indigenous groups live. "It afflicts over seventy five percent (75%) of the population, eighty-six percent (86%) of the rural population, and seventy percent (70%) of female-headed households (forty-nine percent (49%) of which are in extreme poverty).¹" Extremely harsh topography, limited communications and transportation systems, poor quality and uneven distribution of land, and limited services have kept substantial elements of the population in extreme poverty. An outstanding feature in terms of poverty is the inequality that exists in income/consumption and landholding. Some of the major social-economic indicators that reflect this are the following:

1.1 *Distribution of Income:*

The population with the highest ten-percent (10%) income receives 46% of the total income while forty-percent (40%) of the poorest population receive only 7.9% of the total income.

• **Table 1: Distribution of Income**

Lowest 20%	Second 20%	Third 20%	Fourth 20%	Highest 20%	Highest 10%
2.1	5.8	10.5	18.6	63.0	46.6

Source: World Development Report 1998/99, The World Bank

1.2 *GINI Index*²:

The International Bank for Reconstruction and Development reports that Guatemala has the second-worse Gini indicator among sixty-four (64) low to middle income countries. The GINI coefficient for Guatemala is also the highest for Central America.

¹ See the International Bank for Reconstruction and Development, "Guatemala: Second Social Investment Fund Project, Project Appraisal October" 26, 1998, page 3.

² The Gini index measures the extent in which the distribution of income among individuals or households within an economy deviates from a perfectly equal distribution. A Gini index of zero would represent perfect equality, and an index of 100 would represent imperfect inequality (one person or household accounting for all income).

• **Table 2: GINI Index for Central America**

Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua
47.0	49.9	59.6	53.7	50.3

Source: World Development Report 1998/99, The World Bank

1.3 Adult Illiteracy Rate:

The adult illiteracy rate in Guatemala is the highest of Central American Region as may be observed in table No. 3.

• **Table 3: Adult Illiteracy Rate for Central America, 1995**

Costa Rica		El Salvador		Guatemala		Honduras		Nicaragua	
Male	Fem.	Male	Fem.	Male	Fem.	Male	Fem.	Male	Fem
5%	5%	27%	30%	38%	51%	27%	27%	35%	33%

Source: World Development Report 1998/99, The World Bank

1.4 Land Distribution:

The 1995 World Bank report on poverty in Guatemala states that the 1979 agricultural census indicates that two point five percent (2.5%) of the 5.3 million farms in Guatemala, control sixty-five percent (65%) of the agricultural land, with an average farm size of two hundred (200) hectares. On the other extreme, sixteen percent (16%) of the land is cultivated by eighty-eight percent (88%) of the smallest farmers with an average farm size of 1.5 hectares. Guatemala has a Gini Index for land distribution of eighty-five percent (85.9%). This was the third highest index in Latin America.

1.5 Malnutrition

Malnutrition may also be used as a proxy indicator for income at the SO 4 level. The critical assumption is that an increase in the incomes of women micro entrepreneurs will translate into increased consumption for their children. If we compare malnutrition in children of five years old or less with selected countries in the Latin America, we find that Guatemala has one of the worst scenarios as can be observed in table number 4.

• **Table No. 4: Malnutrition in Selected Countries**

Country	Severe	Total
Guatemala 1998/99	21.2	46.4
Haiti 1994/95	14.9	31.9

Country	Severe	Total
Nicaragua 1998	9.2	24.9
Peru 1996	8.0	25.8
Bolivia 1998	9.4	26.8

Source: Guatemala, Encuesta Nacional de Salud Materno Infantil 1998/99.

Malnutrition for the children of the Indian population in Guatemala is 67%. If you exclude Alta Verapaz and Quetzaltenango, at least two children out of three in the Guatemalan Highlands suffer from chronic malnutrition.

As a result of the Peace Accords, large numbers of refugees and displaced populations returned to remote areas placing additional pressures on basic services and the socio-economic infrastructure. One of the immediate challenges facing the Government of Guatemala (GOG) is to increase economic opportunities for the returning and displaced populations in order to rebuild the economic and social fabric after thirty six (36) years of internal conflict. The Peace Accord lays the foundation and the commitments of the GOG to promote sustainable and equitable development programs. The Peace Accords offer USAID/Guatemala the opportunity to assist in supporting and developing microenterprise activities which are owned and operated by the poor, and to improve enterprise performance and household income.

2 Relationship to USAID's and Mission's Strategy

"The U.S. Agency for International Development (USAID) supports microenterprise development to advance its strategic objective of expanding economic opportunity and access for the poor – specifically, the many poor people who operate or work in micro enterprises."³ One of the elements utilized by USAID in combating poverty is to provide access to financial services. Most of the micro entrepreneurs in Guatemala do not have access to savings and credit services provided by the banking sector. Those savers with small accounts that have access to savings are paid interest rates below the inflation rate. In 1998, the commercial banks were paying 4.87% on savings accounts while the inflation rate for the year was 7.48%. On the other hand, most micro enterprises do not have access to credit resources since they lack adequate collateral.

2.1 Agency and Bureaus Goals

The Microenterprise activity for the Poor supports the Agency's goal of encouraging broad-based economic growth and USAID's Microenterprise Initiative. The primary development

³ *Microenterprise Development Policy Paper, U.S. Agency for International Development, page 1, 1995.*

goals for the Micro Enterprise Initiative are to:

- Assist the poor to increase their incomes and assets.
- Increase skills and productivity to enhance economic growth.
- Support sustainable organizations that provide resources to disadvantaged groups.

In June of 1994, USAID launched the Microenterprise Initiative, which commits the organization to four basic principles in the design and implementation of micro enterprise activities. These are:

- Maintaining focus on women and the very poor.
- Helping implementing organizations reach a greater number of people.
- Supporting institutional sustainability and financial self-sufficiency among implementing agencies.
- Seeking improved partnership with local organizations in the pursuit of microenterprise development.

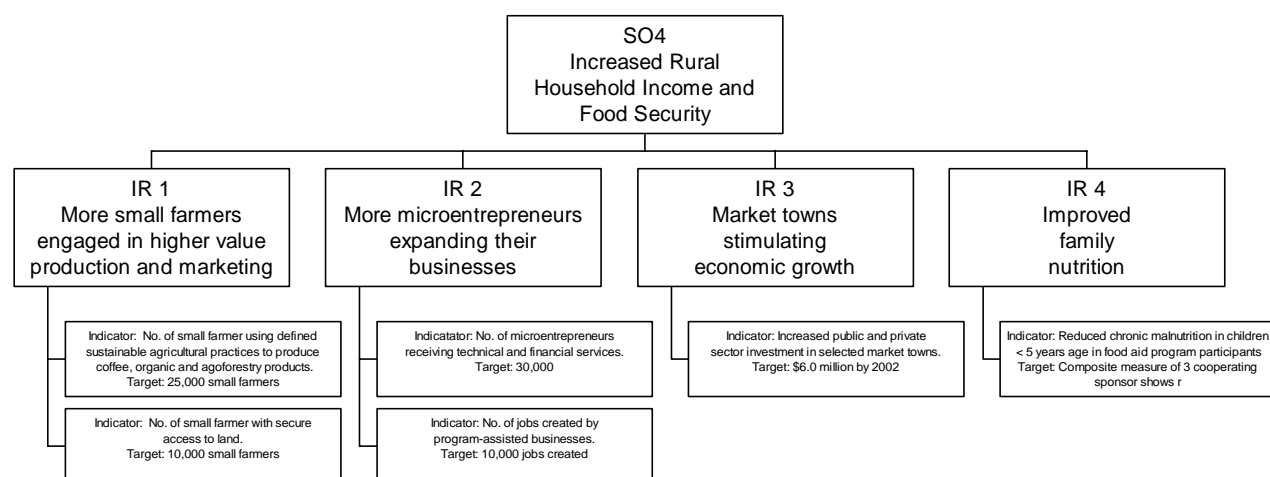
The strategy presented in this document is consistent with USAID's Microenterprise Development Policy Paper and seeks to support a steady movement of a sustainable financial intermediation system that will provide full financial services to micro enterprises. The strategy seeks to promote financial deepening, introduce best practices and promote a large-scale expansion of clients and geographical areas served by unregulated and regulated microfinance intermediaries.

2.2 Missions Strategic Objective (SO) No. 4

The primary objective of the SO 4 is to increase the capacity of a significant number of poor rural families, particularly women and indigenous people, in selected areas of the country to improve their income. Merely increasing income is not sufficient. Generating sustainable increases in incomes requires growth in the economic activities underlying household incomes. USAID/G-CAP seeks to help poor families achieve increases in incomes over time. Temporary or short-term increases in income would not be considered a program success.

Achieving improved household income and food security is dependent upon success in achieving the following four intermediate results as shown in the framework that follows.

RESULTS FRAMEWORK FOR
STRATEGIC OBJECTIVE NO. 4



Improvements in income can be evidenced directly by actually measuring changes in income, savings, the occupational status of the program clients, and through indicators of socio-economic improvement. Broader indicators of sustained income growth in the target geographic areas can be found in the income, occupation, and socio-economic indicators of household surveys.

The microenterprise strategy contributes directly toward the advancement of the Intermediate Results (IR) No. 2, more microentrepreneurs expanding their businesses. The activities assisted by USAID/G-CAP will encourage selected financial intermediaries to expand their geographical coverage, increase the number of clients and portfolio size to attain financial sustainability within a limited period. Best practices will be introduced to the microfinance institutions to assist poor people to increase their incomes and assets, to improve their welfare.

2.3 The Institutional Intermediaries and Clients

There are two levels of customers. The institutional intermediaries and the micro enterprise clients served by the intermediaries.

2.3.1 Financial Intermediaries

There are two major types of institutional intermediaries. The organization that deals primarily with the informal and rural sector customers composed of unregulated not for profit Private Voluntary Organizations (PVOs) and the savings and loan cooperatives that operate through out Guatemala. The second category refers to the regulated financial intermediaries known as commercial banks. In this paper, the financial intermediaries that have financial programs directed toward the informal sector market will be called microfinance intermediaries.

2.3.1.1 NGOs/PVOs⁴:

In Guatemala, there are approximately 400⁵ non-governmental organizations (NGOs). Approximately 30 of these NGOs provide financial services to micro and small business. Of these, only one (GENESIS Empresarial) is financially sustainable. There is however, a small group of NGOs that needs technical assistance and additional liquidity to become financially sustainable within a relative short period. USAID/G-CAP will work with approximately **five or six** of these NGOs to ensure adequate coverage and services for microenterprises at the national level **with special emphasis in what is known as the Zona Paz⁶ (Peace Zone)**.

2.3.1.2 Savings and Loan Cooperatives

The savings and loan cooperatives are a natural partner for USAID in its quest to ensure that poor people have access to financial services. The Guatemalan cooperatives are rural based. About 80% of the cooperatives are located outside Guatemala City. USAID/G-CAP has invested significant resources in strengthening the National Credit Union Federation (Spanish Acronym: FENACOAC), to expand its membership, capitalize the affiliated cooperatives and develop new financial products for its members. As of March 1999, FENACOAC had 31 affiliated cooperatives with a membership of 207,714 persons. USAID/G-CAP will provide technical assistance, training and limited resources to induce FENACOAC and its affiliate to initiate an aggressive microenterprise program.

2.3.1.3 Commercial Banks

As of April 1999, there were thirty-four (34) commercial banks in Guatemala⁷ with one thousand twenty (1,020) branches throughout the country. Despite the relative large branch network, nearly ninety percent (90%) of the loans are disbursed in the Department of Guatemala as may be observed in table number five (5).

⁴ The term non-governmental organizations (NGOs) and private voluntary organizations (PVOs) will be used interchangeably in this document

⁵ Gabriela Braun, Eckart Oehring, *Informe Breve de la Mision de Identificacion 05, Componentes Servicios Financieros*, (Cooperacion Guatemala-Alemana, April 23, 1999), p.5.

⁶ The Zona Paz priority areas defined by USAID/G-CAP consist of the following areas: San Martin Jilotepeque, San Jose Poaquil, Rabinal, Chisec, San Pedro Carcha;, Santa Cruz El Quiche, Ixcán, Nebaj, San Mateo Ixtatan, San Jose and La Libertad. These 12 municipalities have a total population of nearly 600,000 people, or about 6% of the population of Guatemala. See map in attachment D.

⁷ According to the Superintendency of banks, two new banks are in the process of opening operations while a third bank request is under study.

• **Table 5: Loans Disbursed by the Commercial Banks, Q000s**

Description	1993	1994	1995	1996	1997	1998
Guatemala	3,205,574	4,601,051	5,857,031	5,184,487	8,477,451	8,662,555
Total	3,759,891	5,401,784	6,540,895	5,733,685	9,273,097	9,733.494
%	85.26%	85.18%	89.54%	90.42%	91.42%	89.00%

Source: Boletín Anual de Estadística del Sistema Financiero 1998, Superintendencia de Bancos, Guatemala

The fierce competition for the limited number of corporate customers is forcing some of the banks to look at alternative means to increase profits and clients. Some of these banks have started to analyze the convenience of providing services to the large informal sector as a way to increase revenues and expand their outreach through financial deepening. The SO4 team plans to work and provide technical assistance **to four (4) commercial banks⁸** so they may begin to provide financial services to micro enterprises.

2.3.2 The Clients (Micro Enterprises)

There is very limited information on the size of the informal sector in Guatemala. No national survey has been conducted to determine the number of micro and small businesses and the amount of people that work in the informal sector. Some attempts to calculate the number of micro enterprises in the country put the numbers within a range of seven hundred thousand (700,000) to one million (1,000,000). The Program to Support the Informal Sector in Guatemala (Spanish Acronym: PROSIGUA) estimates that there are 797,800 self employed microentrepreneurs and about 26,600 firms which have less than five 5 employees. Assuming that these firms have on the average have 2.5 employees, this means that the total amount of people working in the micro entrepreneur sector are about **864,300, or 26% of the economically active population**. This percentage is consistent with a 1996 survey contracted by USAID in Honduras, which estimated that 25% of the population in Honduras were employed by micro and small businesses. A similar study financed by USAID in the Dominican Republic in 1994 concluded that approximately 25.1% of the EAP was employed by micro and small businesses.

The SO 4, through the IR 2 will assist micro businesses that are typically informally organized. The businesses are owned and managed by people broadly categorized as the working poor including Mayan women, returnees, demobilized ex-combatants and internal displaced persons. The IR2 clients are persons having low incomes, little education, limited or no access to commercial credit, and mostly operating family owned or cooperative businesses. According to USAID policy, it is expected that women

⁸ The four commercial banks that have expressed interest in working with USAID to further their financial deepening process are: BANCAFE, Banco Empresarial, BANRURAL and BANCASOL.

entrepreneurs will receive at least fifty percent (50%) of all loans. Many assisted micro enterprises will generally consist of self-employed persons including unpaid family workers. There is no single definition of micro enterprise, but as a general policy, USAID has adopted the threshold of ten (10) workers, which includes the owner and family members.

2.3.3 Geographical Coverage

There are no restrictions in the geographical coverage supported by the micro enterprise strategy. USAID/Guatemala supports a viable intermediation system that will provide access to financial services to micro and rural businesses. The PVOs need to have a balanced portfolio that will reach a large number of customers at the national level to become financially sustainable. USAID/Guatemala however, supports a comprehensive strategy that includes interventions in the Zona Paz secondary market towns as part of its commitments under the Peace Accords. To support this commitment, USAID/G will give priority to the secondary market towns in the Zona Paz. USAID/G will promote microfinance intervention in the selected secondary cities by creating an incentive fund that will give additional weight to those PVOs that disburse funds in the Zona Paz.

Six of the country's poorest departments have been identified by USAID/G-CAP for the implementation of income generating activities. "These include Chimaltenango, Huehuetenango, Quiche, Alta Verapaz, Baja Verapaz and El Peten. These areas are poor because of a combination of factors such as: isolation, difficult terrain, limited infrastructure, civil conflict, limited marketing opportunities, limited human capital, and limited institutional presence."⁹ These six departments have approximately 27.7% of Guatemala's population. The departments fall between the lower half and the lowest third of the country's 22 departments in terms of basic indicators of human development (IDH), social development (IEDS), and the status of women (IDM).

3 Major Constraints Faced by Microfinance Intermediaries

3.1 PVOs:

3.1.1 Institutional and Financial Sustainability:

Most of the PVOs in Guatemala are relatively weak financial intermediaries and are not financially self-sufficient.¹⁰ Some of the major institutional constraints faced by microfinance intermediaries are: (1) the lack adequate financial policies; (2) high administrative costs; (3) small number of clients and portfolio; (4) lack of adequate

⁹ USAID/G-CAP, *Strategic Objective 4, Increased Rural Household Income and Food Security, Results Package Framework*, 1999.

¹⁰ A financially sustainable PVO is one that collects sufficient revenues to cover the full opportunity costs (or market value) of its activities.

management and technical staff; (5) limited access to commercial sources of funding; (6) weak controls and; (7) inadequate reporting systems.

3.1.2 Focus:

The PVOs in Guatemala with a few exceptions offer a variety of services, such as: credit, technical assistance, training, natural resources management, health and nutrition, etc. The PVOs call this an integrated approach to development. The number of different activities distracts the PVOs from adequately focusing or developing a coherent strategy for sustainability that includes financial services with economies of scale for a large number of micro enterprises. These organizations typically become grant driven institutions involving themselves in an array of projects financed by the donor community. The personnel is not able to specialize in microfinance given the multitude of programs. In addition, most of the personnel have social science background¹¹ with very little understanding of finance.

3.1.3 Access to Financial Resources and Regulatory Constraints:

One of the main issues confronted by microfinance PVOs is the need to access additional market resources to finance their expansion plans to reach a larger number of clients and become sustainable institutions. Microfinance institutions are not allowed to offer savings instruments demanded by their clients because they are unregulated financial intermediaries¹². Reporting standards and financial performance vary considerably from one institution to the next. The formal financial sector perceives these institutions as high risk with a low probability of being profitable. Consequently, most of these institutions have very limited access to market sources of funding. In addition, the regulatory authority does not understand the nature of the microfinance business.

3.1.4 Interest Rate Ceilings:

The Ministry of Economy and the Social Investment Fund (Spanish Acronym: FIS) impose interest rate ceilings on the microfinance intermediaries that receive funds from these two organizations. In the case of the FIS, they currently have an interest rate ceiling of three points above the savings mobilization rate¹³. Given the small portfolio size of the PVOs, the allowed spread does not permit PVOs to cover all costs associated with the loans. This impacts directly on the sustainability level of the PVOs and affects the competitiveness of other PVOs that are charging higher rates in the same market.

3.2 FENACOAC

¹¹ *International Management and Communications Corporation, "Evaluacion de la Metodologia de Bancos Comunes de Mujeres Rurales en Guatemala," n.d., pag. 32*

¹² *It would be irresponsible to recommend that the PVO community be permitted to mobilize savings, given their present institutional development state. A financial restructuring and implementation process has to take place before these institutions develop the capacity to mobilize resources.*

¹³ *Ibid., footnote 10, page. 26.*

As of March 1999, the National Federation of Savings and Loan Cooperatives (Spanish Acronym: FENACOAC) had 31 affiliated cooperatives with 207,714 associates.

3.2.1 Institutional Development:

When you examine the loans in arrears of the affiliated cooperatives, you can clearly distinguish three efficiency levels of intermediaries. In category one, you have seven cooperatives with less than 5% of loans in arrears. In the second category, you have thirteen cooperatives that have between 5.1% and 10% of loans in arrears. In the third category, you have twelve cooperatives that have loans 10% or more of their portfolio in arrears. Within this group, you also have four cooperatives that have 15% or more of their portfolio in arrears.

The World Council of Credit Unions (WOCCU) and the Consultative Group to Assist the Poor (CGAP-World Bank) are providing technical assistance to FENACOAC in the development of a rating and self-regulating system similar to the one proposed in section 5.3 for the PVOs. With this system in place, FENACOAC intends to provide technical assistance for financial and institutional development to the smaller and weaker cooperatives.

3.2.2 Methodology:

To improve the possibility of servicing the micro and small businesses the cooperatives have to adopt new loan methodologies to work with this sector. The cooperatives need to deviate from their normal business procedures of approving loans. Often the top secured limit of a loan may not exceed a percentage of the equity that the member has paid-in the cooperative. This policy has to be balanced out against the borrower's track record and business returns.

3.2.3 Treasury:

While the banking system in Guatemala has been relatively illiquid, FENACOAC has been able to attract a relative large amount of savings¹⁴ from its members. For example in March 1999, the FENACOAC network had a loan portfolio of Q549.6 million, while its savings and equity equaled Q738.7 million. The General Manager requested technical assistance to develop the treasury functions of the financial division, to adequately invest the excess liquidity of FENACOAC.

The issues presented by FENACOAC may easily be turned around to support microenterprise development in Guatemala. See section 5.3.2.

3.3 Commercial Banks

¹⁴ In March 1999, FENACOAC had Q 551,747,017 in savings from its members which represented approximately 5% of the savings of the commercial bank system.

Competition for corporate customers in Guatemala is intensive. As an alternative money making strategy, some of the smaller banks as well as progressive banks are starting to look for new market segments to expand their customer base with new financial services. One of the main issues that the banks face is a lack of knowledge of the small and micro business market. Microenterprise loans are perceived as too high risk and unprofitable. In addition, the commercial banks do not have adequate methodologies for financial deepening. The administrative and operational structure as well as the corporate culture of the banks needs to be adjusted to make small and micro business lending a profitable venture. New financial products have to be developed for this unique market.

4 Constraints Faced by Micro Enterprises:

The constraints faced by micro enterprises have been widely discussed in the development literature. Some of the major obstacles faced by these businesses are the following:

- access to commercial credit at competitive rates due to inadequate guarantees;
- marketing information (business linkages);
- access to good quality inputs in the process of production;
- lack of management skills and;
- lack of legal knowledge to deal with the GOG in areas that involve taxes, labor and legal registration procedures.

5 USAID's/G-CAP Vision, Objective, Strategy, and Activities

5.1 Vision:

A significant number of micro enterprises at the national level have access to full financial services, through a network of profitable intermediaries

5.2 Objectives of the USAID/G Strategy:

- Improve access to financial services for micro and small business.
- Improve financial deepening by strengthening and expanding an institutional system to increase the outreach of the financial intermediaries in a profitable manner.
- Encourage the regulatory authorities to establish a microfinance regulatory framework to promote savings mobilization.

5.3 Reforming and strengthening the Microfinance Intermediaries (PVOs)

As previously stated, most of the PVOs in Guatemala are relatively weak institutions with management deficiencies, limited outreach capabilities, small loan portfolios and currently are financially unsustainable. The focus of the assistance under the microenterprise strategy is to improve the financial and administrative controls and management efficiency of selected PVOs so that they may become profitable institutions providing access to credit to a large number of clients at the national level. USAID will reduce its technical assistance costs to microfinance intermediaries by standardizing the process for institutional development. This way USAID will assist selected organizations achieve large-scale outreach and financial sustainability. Organizations like ACCION International and FINCA International have standardized their technical assistance package to their affiliates with great success. The Mission will embark on the institution building process by standardizing our assistance using the best practices in the field.

To standardize our assistance and improve the effectiveness of the microfinance intermediaries USAID/G-CAP will support the following activities listed below.

5.3.1 Rating System

The creation of a rating system will be used to assess the institutional development stages of the selected institutions. From this analysis, a strategic business plan will be developed to financially restructure the PVOs so that in a period of approximately three (3) years they will become financially sustainable. This business plan will include a technical assistance and training plan that will be implemented by the microfinance intermediary. The analysis will be performed by an institutional contractor that will be selected by the Mission under the SO4. The contractor will perform an analysis of various PVOs and select approximately **six (6) for financial restructuring**. The selected microfinance intermediaries will be evaluated using an adapted Capital Adequacy, Asset Quality, Management, Earnings and Liquidity (CAMEL) risk assessment methodology.¹⁵ The institutional contractor will develop guidelines for the weighted evaluation factors so the microfinance intermediaries may measure their own progress. This rating system will later become the basis for the self-regulating system and eventually a formal supervision by the

¹⁵ The CAMEL rating system was developed in 1978 by the Federal Reserve, the Comptroller of the Currency and the Federal Deposit Insurance Corporation in a coordinated effort to standardize the method of monitoring and evaluating financial institutions.

Superintendency of Banks, if the GOG regulatory authorities so choose. In addition, the rating system will determine the price of funds that the financial intermediaries will pay under the incentive fund.¹⁶

5.3.2 Self-regulating System

After the ratings system has been established, the Institutional Contractor will assist in the development or strengthening of a self-regulating effort. Currently, FENACOAC is creating a self-regulating agency that will supervise its affiliated savings and loan cooperatives. FENACOAC has also expressed interest in performing this role. The institutional contractor will assess the convenience of using this mechanism or an alternative mechanism to introduce prudential supervision and regulatory standards in the microfinance PVOs.

The Superintendency of Banks as well as the Ministry of Economy will be invited to participate in the self-regulating mechanism. The purpose of this is two fold: (1) to introduce the regulatory authorities to microfinance and (2) to motivate the authorities to promote prudential microfinance supervision and a regulatory framework.

The self-regulating mechanism will assist in the introduction of standardized internal controls and reporting systems in the PVO microfinance community. It will also help promote the achievements of financial sustainability, address issues of the ownership structure, operational oversight and prepare the institutions to mobilize savings resources in the future.

5.3.3 Incentive Fund

To accelerate reforms within the microfinance PVOs, USAID/G-CAP will establish an incentive fund that will reward the PVOs that implement the recommended changes that lead to financial sustainability and increased customer outreach. The PVOs that will be assisted by USAID/G-CAP have not reached financial self-sustainability. To achieve sustainability, these microfinance intermediaries need to expand their program outreach and improve the returns of their loan portfolios. The PVOs must continue to modernize their systems and procedures, increase productivity, improve cost-effectiveness of their services and maintain an acceptable level of loans in arrears.

The incentive fund will support this effort by rewarding those PVOs that implement the reforms in a timely manner and maintain acceptable financial performance standards. The targets and performance indicators identified in the strategic business plans will serve as trigger points for access to the incentives. PVOs who meet the planned targets will receive an incentive in the form of a financial bonus on the outstanding loan portfolio financed by the incentive fund. The PVOs that do not meet the targets will not receive the incentive.

The key performance indicators that will be used in the incentive plan are:

¹⁶ See section 5.33 and Attachment A for a full explanation of how the Incentive Fund will work.

- number of active clients and geographical areas served;
- level of financial self-sufficiency;
- quality of the loan portfolio;
- office and field productivity; and
- cost-effectiveness structure of the organization.

A detailed incentive program will be designed by the institutional contractor and approved by USAID/G-CAP prior to its implementation. Attachment A describes the major elements that will be considered in the incentive fund.

5.4 FENACOAC

5.4.1 Role as Rating and Supervisory Agency:

FENACOAC requires relatively little technical assistance to play a key role in micro enterprise development. As discussed previously, the institutional contractor will assess the convenience of using the rating and self-regulatory system that is being developed to supervise the affiliated cooperatives. If agreement were reached with FENACOAC, the PVOs would then pay a fee for this service. The institutional contractor will work with FENACOAC to make the necessary adjustments to the rating and supervisory norms to ensure that they are compatible with the financial structures of the PVOs.

5.4.2 Methodology:

The institutional contractor will provide technical assistance to FENACOAC to introduce micro credit technology in the cooperatives. The institutional contractor will sponsor some study tours abroad to examine best practices in microfinance. In addition, some training seminars will be conducted so the FENACOAC personnel may train the personnel in the cooperatives in microfinance.

5.4.3 Treasury, New Financial Products and Observation Trips:

The institutional contractor will assist FENACOAC in the development of its Treasury functions with special emphasis on the investment of its excess liquidity. The institutional contractor will assist in developing the custodial functions of the resource documentation, investment function, cash and liquidity management, and, lending operations to microfinance PVOs. The FENACOAC General Manager has expressed his particular interest to channel financial resources to the microfinance PVOs at market rates. This is a welcome step for the development of financial linkages between intermediaries.

USAID/G will provide technical assistance to FENACOAC to develop new financial products. Some of the areas identified by the General Manager of FENACOAC are the

following: (1) credit methodologies for financial deepening; (2) savings instruments; (3) leasing¹⁷; (4) credit cards; (5) and development of a clearing house¹⁸ for the savings and loan cooperatives.

USAID/G will support observation trips abroad to support exchange of experience and introduce best practices. These trips will be utilized to learn about new microfinance products and techniques being used by organizations in the microfinance frontier. This type of activity is essential to improve the technical skills, introduce new concepts, and improve the knowledge base of our Guatemalan partners. These trips will assist FENACOAC in the development of new financial products and to have a better understanding of the operational changes that are required to introduce new activities within FENACOAC and its affiliated cooperatives.

5.5 Attract Commercial Banks into Microfinance

The strategy and activities will focus on ways to improve financial deepening of the commercial banks and promote an efficient and competitive system for microfinance. To support the strategy USAID will finance the following activities:

- Observation and study tours abroad for key bank personnel to see successful programs in the Dominican Republic (BANCO ADEMI), Bolivia (BANCOSOL), Panama (Multi-Credit Bank, Financiera EstrellaMar), El Salvador (Financiera CALPIA) and other countries as warranted. The senior bank representatives will have an opportunity to speak with their peers and understand that microfinance activities are a profit making opportunity.
- Technical assistance and training will be provided to introduce lending methodologies and required operational adjustments in the banks.
- The development of new financial products will be supported to improve the financial services for the microenterprise sector and reduce the transaction costs of doing business. Some of the technical assistance requested by the banks in this area includes, credit card operations (having their own credit card brand), the introduction of smart cards, and savings mobilization instruments. The experience of these instruments by other institutions will be examined before the design and implementation of the new products. Interested institutions (such as BANCAFE, BANRURAL, GENESIS and others) will visit a finance company in Panama (Financiera Estrella Mar) that uses the credit card brand system to provide financial services to over 15,000 active clients with a staff of 16 persons. This paperless activity reduces the transaction costs, increases profits for the financial intermediary and reduces the financial costs to the borrower. A second institution that will be visited is a commercial bank in Honduras (BANCOFUTURO) that uses the intelligent card system.

¹⁷ Leasing is a form of contract transferring the use of equipment, land, etc. in consideration of payment in the form of rent.

¹⁸ The principal purpose of the clearinghouse is to facilitate the clearance and settlement of checks payable.

- USAID will provide technical assistance to BANRURAL in the development and implementation of a strategic plan. BANRURAL has requested technical assistance to improve the management of its branches, and move its portfolio toward a second-tier facility.¹⁹
- Several instruments are being and will continue to be utilized by USAID to entice banks into microfinance. These include the Loan Guarantee Program managed by USAID/W. Under this program, Banco Empresarial has authority to issue \$2.0 million worth of bonds. Fifty (50%) percent is guaranteed by the U.S. Government. In addition, with USAID's Development Credit Authority, the Mission will commit limited resources to guarantee 50% of the micro and small business loan portfolio of banks that will support a financial deepening program with special emphasis outside the city of Guatemala.
- USAID will inject short-term financial resources that will be used by selected PVOs under the incentive fund structure described in attachment A. The incentive funds will be managed through a trust arrangement that will be competed in the commercial banking system. Both BANRURAL and BANCAFE have expressed their interest in managing this trust fund.

5.6 Other Policy Dialogue and Activities:

5.6.1 Influencing Reforms in the Financial Sector

5.6.1.1 Microfinance Regulatory Framework

The Mission will develop a policy agenda to discuss relevant issues that affect on and off farm production and promote a dialogue with the regulatory authorities to support micro and rural finance activities. One of the main topics in the area of microfinance is prudential supervision and regulation. USAID will fund activities (such as travel to visit the Superintendency of Banks in Bolivia and Peru, short-term technical assistance and training) to improve the understanding of regulatory authorities as to the specialized nature of micro enterprise financial services. Through the institutional contractor and USAID staff, we will provide support to a task force with public and private sector representatives to assess the convenience of establishing a regulatory framework for microfinance.

5.6.1.2 Legal Issues

The PVOs complain that there are major issues related to obtaining title of the assets used as collateral in case of default. USAID will promote a dialogue concerning contract enforcement issues related to assets used as guarantees. If necessary Guatemalan legal services will be contracted to review the issue and make recommendations.

¹⁹ *BANRURAL has a serious contradictory problem with its strategy since it wants to expand its branch outreach and at the same time move most of its operation to a second-tier facility.*

Most loans disbursed to micro enterprises are guaranteed by a group of borrowers²⁰ or by the assets that are purchased from the loans. Formal financial institutions are required to maintain adequate ratios between the outstanding loan portfolio and the guarantee that secure these loans. This discriminates against the small borrower since most of the methodology used to service the poor require group guarantees; i.e., if one person does not pay the rest of the group will pay. Formal financial institutions like Banco Empresarial have reported that they are affected by this policy. This issue is also compounded by the fact that only certain types of assets may be used as guarantees for the loans, since the procedure to register the collateral is costly and cumbersome. This issue particularly discriminates against the small borrowers. USAID will assist the Superintendency of Banks in understanding how this negatively impacts on the smaller borrowers. A study trip to the Superintendency of Banks in Bolivia would assist the GOG in adopting a flexible guarantee policy that would not put the small borrowers at a disadvantage.

5.6.1.3 Financial Repression

Some of the microfinance intermediaries report that GOG programs encouraged by donors set upper interest rate ceilings. USAID will meet with GOG Officials and the Donor community to discourage this practice. Microentrepreneurs and poor people need access to financial services, not subsidies. The only way that they will have access to permanent financial services is by permitting the intermediary to have a full cost recovery policy with a market driven vision. Subsidies encourage investment in activities that are not sustainable under market conditions. In addition, it sends the wrong signal to the borrowers (funds do not necessarily have to be paid back because they were a grant). Efficient financial intermediaries need to charge competitive rates to cover all transaction costs to become sustainable. Interest rate restrictions should be removed.

5.6.2 Promoting Product Development and New Financial Services

USAID will support efforts to develop a strategy to mobilize savings from the informal sector and business community in general. In addition, other types of financial instruments that will be explored jointly with the microfinance intermediaries are equity financing, leasing and insurance. We will examine these and other instruments to determine what is appropriate and implement their use in the microfinance community.

5.6.3 Developing Linkages with the Capital Markets

There is a huge unmet demand for microfinance services. One of the connections that needs to be developed to partially service a relatively important part of this demand is linkages with the capital markets and formal financial intermediaries. USAID/G-CAP has already started to encourage intermediaries with its Loan Guarantee Program (LGP). For example, in September of 1997, USAID signed a guarantee agreement with Banco Empresarial. The agreement permits Banco Empresarial to issue Guatemalan currency

²⁰ *This is because solidarity lending and village banking methodologies use groups lending to reduce the transaction cost.*

denominated debt instruments (bonds) equivalent to \$2,000,000²¹. Banco Empresarial used the resources from the bond issuance to increase its lending to micro and small businesses in Guatemala. USAID should continue to support the broadening and deepening of the Guatemalan capital markets by encouraging banks to issue longer-term debt instruments as a stable source of funding for micro and small business lending. USAID/Guatemala should continue to encourage the use of the LPG managed by USAID/W for this purpose.

The Development Credit Authority (DCA) is another instrument that may be utilized by the SO 4. The DCA gives the additional flexibility of permitting the financial intermediaries to lend the mobilized resources under its guarantee to any sector, thus effectively responding to market needs. This instrument may be invaluable to activities supported under the (IR3) INDUPAZ Program. It may be used to encourage the formal financial sector to provide financial services to businesses that invest in the Zona Paz. The instrument is also useful to help establish profitable linkages between the formal financial sector and microfinance intermediaries. Under the DCA, USAID is authorized to provide direct loans to financial intermediaries and/or loan guarantees on the outstanding portfolio that contributes to the strategic objectives set out in the contract. Given the limited management resources and amount of new and on-going activities, this instrument will be accessed during FY 00.

5.6.4 Promoting Research and Key Studies

USAID/G-CAP will fund research and specialized studies on key areas of interest. Some of the studies may be longitudinal studies to improve our understanding of the size and dynamics of the sector. Other studies may be related to legal issues in microfinance, such as, problems in the law related to the control and use of moveable goods as collateral. Research may also be carried out to fine tune the regulatory framework and improve the understanding of the regulatory and monetary authorities in the specialized nature of microfinance. Financial markets issues will be assessed to continue the policy dialogue with the Government of Guatemala and other donors.

5.6.5 Training to Microfinance Trainers

USAID/Guatemala will support some training and technical assistance so that the microfinance intermediaries may provide non-financial services directly to micro and small businesses. The institutional contractor will perform a survey of the customers of microfinance intermediaries and define in order of priority the non-financial services that are demanded by clients. To respond to the clients needs, the Institutional Contractor will define a technical assistance and training plan for intermediaries, so they may implement the assistance requested by their clients. Given the limited amount of resources, USAID will dedicate most of its assistance to support a financially viable system that provides full financial services to the poor. USAID/G will encourage other donors to support the efforts of the intermediaries in non-financial services. In addition, USAID/Guatemala will work

²¹ *Banco Empresarial only issued the equivalent of \$1.0 million worth of bonds due to the existing market conditions in the financial sector. Banco Empresarial has stated that it will float a second bond issue for \$1.0 million.*

with the GOG authorities to identify policy and regulatory issues as well as, institutional and operational bottlenecks that affect the performance of small producers.

5.6.6 Promote Donor Coordination

Contradictory donor policies will undermine USAID efforts in assisting the poor. USAID will promote donor-coordinated activities to support micro enterprise and rural financial services. USAID has already started to coordinate its activity with the IDB and the GTZ. Together with these institutions, we have agreed to hold quarterly coordinating meetings with the major donors in the area of micro and rural finance and discuss policy and strategy amongst the donors. USAID will focus its donor dialogue in the following areas:

- Promote financial policies that reflect market.
- Promote and develop standardized performance measurements (CAMEL) in coordination with other donors.
- Promote and develop the standardization for financial reporting among the donor community.
- Disseminate information on best practices and share studies with the Donor Community, GOG and Practitioners.
- Participate and/or host meetings with the donor community every four months to discuss advances and issues that affect the sector.
- Promote the participation of other donors in support of non-financial services.

6 ILLUSTRATIVE BUDGET

• **Table 4: Illustrative Budget to Support the Microfinance Strategy, In US Dollars**

Description	Amount
PVOs	6,111,574 ²²
FENACOAC	172,246
Commercial Banks	582,328
Policy Reform	176,164

²² Includes the credit fund.

USAID/GUATEMALA MICROENTERPRISE DEVELOPMENT STRATEGY

Description	Amount
Research & Studies	276,164
Training Micro Finance Trainers	97,123
Donor Coordination	10000
Total Estimated Budget	7,425,599

Please see attachment C for the budget detail.

7 ATTACHMENT A: ELEMENTS OF THE INCENTIVE FUND

7.1 Objectives:

The incentive fund will support the following objectives:

- Promote increased access to financial services and client outreach at the national level with emphasis on the Zona Paz.
- Accelerate financial reforms and promote the financial sustainability of the microfinance intermediaries, using best practices.
- Prepare the microfinance intermediaries to become regulated financial intermediaries.
- Improve the quality of the reporting and accountability of the PVOs.

7.2 Focus of the Incentive Fund

- Reward the winners not the losers.
- Improve the outreach (number of clients), geographical coverage and services provided to its clients.
- Strengthen and introduce market financial policies in the PVOs to promote financial self-sufficiency.
- Create a business culture within the PVOs.
- Promote strategic and business planning and implementation in the PVOs.
- Develop efficiency indicators and targets that have to be achieved by the microfinance intermediary.
- Use the incentive fund resources to finance new activities described in the strategic and business plan.

7.3 Major Aspects of the Methodology:

To have access to the incentive fund the organization has to do the following:

- Undergo a CAMEL Analysis and be rated.
- Develop and implement a business plan with clear efficiency indicators and targets that have to be met.

- Prepare monthly financial statements and management reports according to the standardized format that will be developed for this purpose.
- Be subject to an evaluation every six months to see if the indicators and targets are being met.
- The PVOs will pay market rates for the use of the funds. If the PVOs meet the targets and indicators, they will get a bonus. The bonus will be equal to the difference between the market rate and the average savings mobilization cost of the commercial banks plus the weighted average management fee of the funds. The PVOs that do not meet the targets and indicators will pay market rates. The rates may differ for each PVO depending on their classification in the rating system.
- The incentive fund will be managed under a competitive trust arrangement.

7.4 Institutional Contractor

- The institutional contractor will present to USAID/G-CAP a draft incentive fund system for USAID's approval.
- The incentive fund will be managed under a competitive fiduciary agreement with a commercial bank. The institutional contractor will prepare the draft fiduciary contract that will be negotiated between USAID/G-CAP and the selected bank.
- The institutional contractor will prepare an options paper recommending on how to dispose and utilize the incentive fund's resources after the program expires.

8 ATTACHMENT B: BANRURAL

8.1 BANDESA/BANRURAL Background:

In 1997 BANADESA's²³ operation were closed and BANRURAL was created to provide access to rural credit to small farmers and micro enterprises. During 1997 and 1998 BANRURAL went through a successful transition from being formerly the state-owned Agricultural Development Bank (BANDESA) to becoming a mixed-capital bank. In 1998, USAID/W financed a CAMEL analysis since BANRURAL applied for a Loan Portfolio Guarantee (LPG) for \$1.0. The CAMEL evaluation rated BANRURAL as follows:

Description	Rating
Capital Adequacy	(1) Strong
Asset Quality	(3) Fair
Management	(3) Fair
Earnings	(2) Satisfactory
Liquidity	(2) Satisfactory
Overall Rating	(2.2) Satisfactory

As a result of the positive evaluation, BANRURAL signed a LPG Agreement with USAID for \$1.0 million. Under the agreement, USAID guarantees up 50% of a loan portfolio of \$2.0 million. Loans that qualify under this agreement will not exceed \$150,000 for small business and \$5,000 for micro enterprises. For this service BANRURAL pays a facility fee of 0.5% over the maximum limit of the guarantee and 0.5% utilization fee for the outstanding loan portfolio. From April to June 1999, BANRURAL made 4 loans for a total amount of Q372,444 guaranteed by the LPG. It is still too early to determine the impact that the LPG program will have in BANRURAL's loan portfolio. USAID will closely monitor this activity to determine if the guarantee program is permitting BANRURAL to reach customers with viable projects that would not have access to commercial credit due to inadequate or insufficient collateral.

In addition to the LPG recently signed with USAID, BANRURAL manages the Rural Credit Trust that was originally financed by USAID loans and grants. The source of funding for

²³ When BANADESA was closed it had nearly 70% of its loan portfolio in arrears.

the Rural Credit Trust fund may be observed in the following chart.

**RURAL CREDIT TRUST FUND MANAGED BY BANRURAL
ORIGINAL SOURCE OF FUNDING**

Names and Sources of Trust Fund	Amount In Q
Granos Básicos, Diversificación de Cultivos, y Mercadeo de Granos Básicos (AID-520-L-018)	27,513,000
Desarrollo del Movimiento Cooperativo (AID-520-L-024)	5,000,000
Desarrollo de Cooperativas Agrícolas del Altiplano (AID-520-K-036)	3,855,462
Asociación de Mercadeo Integrado por Federaciones de Frutas y Hortalizas (AID-520-T-030)	5,900,000
Desarrollo Agrícola del Altiplano del País (AID-520-T-037)	30,342,876
Sistema de Diversificación para el Pequeño Agricultor (AID-520-T-034)	7,402,022
Colonización de Nuevas Tierras AID-520-T-026)	5,600,000
Mejoramiento de los Recursos de la Tierra (520-T-026)	859,276
Conservación de Suelos y Obras de MiniRiego (PL480-84)	6,037,116
Programas de Centros de Comercialización Agrícola _PCCA- AID Sección 416-87	2,000,000
Total	94,509,752

(Pending: Need financial report of the Rural Credit Fund to analyze usage of the Trust Fund)

In addition to the above, USAID/G-CAP plans to capitalize the Rural Credit Fund with an additional \$3,740,000 in FY 99 and \$3,001,000 in FY00. The source of these funds are the following:

FISCAL YEAR 1999 AND 2000 RESOURCES

IR Number	Income	Peace	Mitch	TOTAL 99	TOTAL 00	GRAND TOTAL
IR 1	500	400	0	900	0	900
IR 2	490	350	2,000	2,840	3,001	5,841
Total	990	750	2,000	3,839	3,001	6,741

Under the Rural Credit Fund, BANRURAL provides credit to financial intermediaries and individual borrowers for agricultural production, micro enterprises and pre-investment activities.

8.2 Issues:

There are various issues that the USAID/Guatemala has to consider before providing additional funds to capitalize the trust fund managed by BANRURAL and owned by the GOG. These are the following:

8.2.1 Level the Playing Field:

The management of the Rural Credit Trust Fund provides BANRURAL a significant advantage over the competition. BANRURAL uses the trust funds to make direct loans to its clients at rates below the market²⁴. The PVO microfinance community cannot compete with BANRURAL on price. This gives BANRURAL an advantage over competitors since it is using GOG trust funds to subsidize its operation. Besides the subsidy, BANRURAL is earning income for the management of the trust fund. If the Mission decides to capitalize the trust fund, the interest rate issue should be negotiated with BANRURAL by requesting that they increase the rate charged to its direct clients to a formula that reflects market.

From its second tier operation BANRURAL lends to financial intermediaries at a 15% rate. Since most of the microfinance intermediaries are relatively inefficient and have a small loan portfolio, they require a relative large spread to cover their costs. This affects their competitiveness vis-à-vis BANRURAL's direct lending.

BANRURAL exercises monopolistic pressure over its clients. For example, FINCA/Guatemala submitted a loan request under BANRURAL's Rural Credit Trust Fund. Before the loan was approved, BANRURAL requested that FINCA sign an operational agreement. The proposed agreement stated that FINCA would transfer its customers to BANRURAL and train BANRURAL's personnel in the management of village banking. This condition is unacceptable from any point of view. The microfinance organizations need their clients in order to become sustainable organizations. FINCA did not sign the proposed agreement and the loan request was turned down for other reasons. This serious issue needs to be addressed with BANRURAL's management before any additional funds are granted to the Rural Credit Trust Fund.

8.2.2 BANRURAL's Strategy:

According to BANRURAL Executives, this institution receives approximately 80% of its revenues from direct credit to businesses and 20% from its second tier lending facility. As part of its strategy, BANRURAL seeks to reverse the sources of its revenues by the year 2003. That means that they plan to receive 80% of their resources from the second tier operation and 20% from direct lending. BANRURAL's strategy however does not appear to reflect their strategy, since they continue to expand their branches throughout the

²⁴ BANRURAL charges the following rates to its customers:

Description	Individual Loans	Solidarity Groups	Com. Banks	Small & Med. Bus.
Amounts	500 to 12,000	500 to 4,000	500 to 4,000	>10,000
Interest Rate	32% over balance	32% over balance	22% over balance	18 to 22% over balance

country. A second tier lending facility does not need a large network of branches throughout Guatemala, since this increases costs unnecessarily. Technical assistance will be provided to BANRURAL to address this operational inconsistency so this organization may achieve maximum impact with the least amount of resources.

8.2.3 Ownership of Funds:

A third issue to be considered by the Mission is the ownership of funds. Should USAID capitalize a trust fund owned by the GOG or should we provide equity grants directly to microfinance intermediaries? There are certain advantages and disadvantages under both alternatives. Some of the major advantages of using the existing trust fund managed by BANRURAL are the following:

- More institutions will have access to the limited amount of resources over a longer period of time.
- Intermediaries have to pay market rates for the use of these funds and financial discipline is introduced. Accessing funds from a second tier facility will prepare the microfinance intermediaries to eventually obtain funds from the financial market.
- The USAID management burden is lowered since one institution will manage the trust fund and lend to other microfinance intermediaries.
- USAID will continue to support the GOG in priority areas through an existing mechanism that is already in place.
- USAID has previous funding commitments that it seeks to fulfill.

On the other hand, there are some questions that we should ask ourselves before continuing to put more resources in the trust funds. USAID has already capitalized this fund with more than Q90.0 million. Is it convenient to put all our eggs in one basket? Should USAID continue to grant funds to the GOG for microenterprise lending? Should the Mission balance its approach and grant funds to the private sector instead of the GOG?

- The Mission's experience with the private sector has been extremely successful. For example, USAID/Guatemala gave a \$2.0 million grant to GENESIS Empresarial. This organization became sustainable in a three-year period. It has since become a viable and profitable organization, serving more than 22,500 active clients with a loan portfolio of more than \$12.1 million by December of 1998. GENESIS is currently in the process of creating a specialized bank to service micro enterprises in Guatemala. In addition, GENESIS Empresarial is one of the leading organizations in microfinance in Latin America. This experience can be replicated with some selected microfinance organization.
- **Management of the Trust Fund:** USAID should compete the management of the resources earmarked for credit in a trust fund agreement. This will undoubtedly take

time to establish. To avoid project delays, USAID/G could temporarily give the resources to BANRURAL to manage within the existing Rural Credit Fund (with some operational modifications as discussed above). This way project implementation will not be halted and the microfinance organizations may have access to the resources. The Mission would then prepare operational procedures for the trust fund and bid the trust within the banking sector. BANRURAL would be invited to participate in the bid along with other interested banks. Once the new trust agreement is set the resources and outstanding loan portfolio would be transferred to the institution that is selected.

- ➡ **Ownership of Funds:** On the issue of resource ownership²⁵, the SO 4 team recommends that the funds be granted to the PVOs after a period of time. To receive this grant, the intermediaries would be evaluated based on impact, in terms of clients served, geographical area covered, quality of the loan portfolio and financial sustainability. The institutional contractor would recommend the terms and conditions of the grant to USAID for its approval during the life of the project.

²⁵ *This assumes that USAID is not obliged to grant the resources to the GOG.*

9 ATTACHMENT C: ILLUSTRATIVE BUDGET

ILLUSTRATIVE BUDGET TO SUPPORT THE MICROFINANCE STRATEGY				
Activity	Description	Months	Unit Cost	Total
PVOs				6,111,574.00
5.3.1 Rating System				80,164.00
- Design the Rating System	Technical Assistance (months)	4	19,041.00	76,164.00
- Visit Honduras to See Rating System	Persons travel (PVOs, Superintendency, Min. of Economy, FENACOAC)	8	500.00	4,000.00
5.3.2. Self-Regulating System	Technical Assistance (months)	4	19,041.00	76,164.00
5.3.3. Incentive Fund	Credit Fund			5,841,000.00
5.4.4 Product Development	Savings, Equity financing, leasing, etc.	6	19,041.00	114,246.00
FENACOAC				172,246.00
5.4.1. Rating/Supervisory Agency	Technical Assistance (months)	2	19,041.00	38,082.00
5.4.2. Methodology for FENACOAC	Technical Assistance (months) and training of personnel	1	50,000.00	50,000.00
5.4.3. Treasury, Product Dev.				84,164.00
- Short Term TA	Technical Assistance (months)	4	19,041.00	76,164.00
- Observation Trips	Visit succesful programs in other countries	4	2,000.00	8,000.00
BANKS				582,328.00
5.5 Commercial Banks				582,328.00
- Observation Trips	Travel Abroad (persons)	15	2,000.00	30,000.00
- Methodology Banks	Technical Assistance (months) and training of personnel	2	50,000.00	100,000.00
- New Financial Products	Technical Assistance (months)	6	19,041.00	114,246.00
- TA BANRURAL Strategic Plan	Technical Assistance (months)	2	19,041.00	38,082.00
- DCA	USAID/G Obligation			300,000.00
- IGP	No Cost to USAID/G			n/a
POLICY REFORM				176,164.00
5.6.1. Policy Reform				176,164.00
- Regulatory Framework	Observation Trips, overseas training, technical assistance and seminars.			100,000.00
- Contract Enforcement (Guarantees)	Technical Assistance (months)	1	19,041.00	19,041.00
- Other Policy Issues Identified by Institutional Contractor	Technical Assistance (months)	3	19,041.00	57,123.00
RESEARCH & STUDIES				276,164.00
Key Studies	Microenterprise Survey			200,000.00
	Proxy Indicator for Employment Generation	1	19,041.00	19,041.00
	Impact Assessment	3	19,041.00	57,123.00
	Seminar on Best Practices	4	10,000.00	40,000.00
TRAINING MICROFINANCE TRAINERS				97,123.00
	Technical Assistance	3	19,041.00	57,123.00
	Training Seminars	8	5,000.00	40,000.00
DONOR COORDINATION				10,000.00
	Meetings and Seminars			10,000.00
Total				7,425,599.00
Minus Credit				5,841,000.00
Balance				1,584,599.00
Minus Institutional Contractor				
Balance				

Estimated Cost for One Month of Technical Assistance

Description	
USAID Max Rate	\$445.00
No. of Work Days Per Month (Assuming a 6 day work week)	26
Max Rate per months	\$11,570.00
Per Diem 31 Days	4,340.00
Travel (Washington Guatemala Round Trip)	1,000.00
Local Travel	400.00
Subtotal	17,310.00
Miscellaneous (10% of Total)	1,731.00
Total Per Month	19,041.00

Note: Does not include overhead but is calculated at USAID Max Rate

10 ATTACHMENT D: MAP OF 12 MARKET TOWNS

KEY GEOGRAPHIC AREAS FOR INCOME GENERATION ACTIVITIES

1.1.1 CHIMALTENANGO

1. SAN JOSE POAQUIL
2. SAN MARTIN JILOTEPEQUE

1.2 BAJA VERAPAZ

3. RABINAL

1.3 ALTA VERAPAZ

4. CHISEC
5. SAN PEDRO CARCHA

1.4 QUICHE

6. SANTA CRUZ EL QUICHE
7. IXCAN
8. NEBAJ

1.5 E. HUEHUETENANGO

9. SAN MATEO IXTATAN
10. BARILLAS

1.6 F. EL PETEN

11. SAN JOSE
12. LA LIBERTAD

